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INTRODUCTION

In accordance with the City Auditor's 1995-96 Audit Workplan, we have audited the operations of the Department of General Services' Fleet Management Division. In connection with this audit, we reviewed the Fleet Management Division's system for developing and using performance standards in repairing and maintaining City-owned vehicles and for determining whether the Division's performance is competitive with private industry and other governmental organizations. We also contacted other jurisdictions that have attempted to privatize their vehicle maintenance functions. We conducted this audit in accordance with generally accepted government auditing standards and limited our work to those areas specified in the Scope and Methodology section of this report.

BACKGROUND

In 1979, fleet maintenance was part of the Public Works Department. Prior to this, the Finance Department managed police vehicle maintenance. In early 1980, the Department of General Services was formed to administer purchasing, vehicle maintenance, and building maintenance.

In 1985, there were four separate city of San Jose (City) departments that were responsible for maintaining the City's automotive fleet and motorized equipment. The Airport, Fire, and Water Pollution Control Departments maintained their own equipment, while General Services' Fleet Management Division (Fleet Management) maintained the balance of the City's automotive fleet and motorized equipment.

It was not until 1989-90 that Fleet Management assumed vehicle maintenance for the Airport Department. This consolidation resulted from a City Auditor's report on the cost to maintain the Airport Department's shuttle buses. This consolidation was successful in that the $1.2 million annual cost to maintain the shuttle buses was reduced to $534,000 per year--an annual savings of $666,000.

A November 1991 study recommended consolidating the Fire Department's fleet maintenance with that of Fleet Management. The study concluded that "*transfer of this responsibility to the Vehicle Maintenance Division (VMD) could be accomplished with a net savings to the City of approximately $104,000 per year.*" Fleet Management took over the Fire Department vehicle maintenance function on July 1, 1993.

Major Accomplishments Of The Fleet Management Division

In Appendix B, the Department of General Services informed the City Auditor's Office of its major accomplishments relating to the maintenance and replacement of police vehicles. In Appendix D, General Services summarized the condition of the Fire Department fleet. Among the major accomplishments of Fleet Management over the past five years are the following:

- Consolidated maintenance and repair of all City vehicles (except Water Pollution Control equipment) within Fleet Management resulting in significant savings and California Highway Patrol compliance for Airport shuttle buses and major improvements in the condition of fire apparatuses.

- Restructured staff and operations resulting in the ability to provide adequate maintenance and repair services for a total growth in fleet size of 30 percent (470 vehicles) without any increase in Fleet Management staffing level.

- Established a warranty recovery program which annually recovers more than $95,000.

- Implemented in-house and factory-sponsored training to keep staff current on new technologies for shop equipment and passenger vehicles and light trucks.

- Restructured interdepartmental billing charges by eliminating the base rate and adopting an hourly labor rate to parallel billing practices in the private sector.

SCOPE AND METHODOLOGY

Our objectives for this report on the audit of the Department of General Services' Fleet Management Division (Fleet Management) were

- To determine if Fleet Management has developed and used performance standards for the repair and maintenance of City-owned vehicles and for assessing Fleet Management's comparative performance with private industry and other governmental organizations and
- To survey other jurisdictions and learn of their attempts to privatize their vehicle maintenance functions.

We interviewed Fleet Management's staff including the fleet manager, the staff analyst, the municipal garage supervisor, the automotive equipment specialist, and the main yard supervisor. In addition, we contacted the following jurisdictions that have privatized their fleet maintenance functions:

- City of Indianapolis, Indiana
- City of Fort Lauderdale, Florida
- City of San Mateo, California
- City of Des Moines, Iowa
- County of Montgomery, Alabama
- County of Los Angeles, California
- City of Winter Park, Florida
- County of Richland, South Carolina

We limited our review to Fleet Management's efforts to develop and implement vehicle maintenance performance standards to assess its operational effectiveness and efficiency and its competitiveness with private industry and other governmental organizations.

Our audit initially included a review of maintenance repair costs, preventative maintenance schedules, customer usage, the fueling system, new car build-up, and inventory. We were unable to complete our review in these areas due to the resignation of the auditor assigned to the audit. We will, however, share with General Services what analyses we were able to complete.

We also performed a preliminary review of Fleet Management's Equipment Management Information System (EMIS). Our review of the EMIS revealed several internal control deficiencies. We did not pursue these internal control deficiencies as an audit finding because Fleet Management is currently implementing a new equipment management system called Prototype Equipment Management System for the IBM Personal Computer Environment (EMS/PC). According to Fleet Management administration, the new system is designed to mitigate most, if not all, of the deficiencies of the old system. Once the new system is implemented, the City Auditor's Office will include an audit of the new system in its proposed annual workplan.

FINDING I

BY DEVELOPING AND IMPLEMENTING PERFORMANCE STANDARDS, THE FLEET MANAGEMENT DIVISION CAN ASSESS ITS OPERATIONAL EFFECTIVENESS AND EFFICIENCY AND ITS COMPETITIVENESS WITH PRIVATE INDUSTRY AND OTHER GOVERNMENTAL ORGANIZATIONS

The Fleet Management Division (Fleet Management) of the Department of General Services (General Services) services and maintains automobiles, light trucks, and heavy trucks for General Services and other city of San Jose (City) departments. Fleet Management charges the departments for which it provides services based upon an hourly rate and the number of hours required to perform the services. As such, it is in the best interest of the departments that Fleet Management provides efficient and effective services that are competitive with private industry and other governmental organizations. Our review of Fleet Management's use of performance standards to assess its competitiveness with private industry and other governmental organizations revealed that

- Performance standards cannot be incorporated into Fleet Management's Equipment Management Information System (EMIS). As a result, Fleet Management has no procedures to either incorporate performance standards into the EMIS or monitor actual performance against established performance standards;
- The performance standards Fleet Management has developed are not used to assess its competitiveness with private industry or other governmental organizations; and
- Fleet Management has not fully implemented its new fleet management system;

In addition, with regard to privatizing the vehicle maintenance function,

- Our review of authoritative sources and surveys of other governmental jurisdictions revealed that vehicle maintenance services can be successfully privatized and

- Obstacles to privatization, such as union resistance, contracting-out pitfalls, and the City Council's current policy on privatization can be overcome.

In our opinion, Fleet Management should expedite the implementation of its new Equipment Management System for the IBM Personal Computer Environment (EMS/PC). By establishing performance standards, developing economic benefit criteria for recommending privatization, and monitoring actual performance against those standards and criteria, Fleet Management will be able to assess if it is functioning economically, efficiently, and effectively and to identify any functions that can be successfully privatized.

The Fleet Management Division Of The Department Of General Services

Fleet Management's mission is to provide authorized users of City vehicles and equipment with safe and dependable vehicles and construction equipment. This includes all City equipment except that of the Water Pollution Control Department.

The program purpose and description states:

> *. . . provide interdepartmental services including the purchase, replacement and repair of vehicle and construction equipment. Equipment is maintained in optimum condition by performing periodic preventive maintenance, scheduled and unscheduled repair work, and supplying fuel and lubricants at support facilities throughout the City . . .*

As of September 1995, Fleet Management indicated that there were approximately 2,250 pieces of equipment in the City's fleet. These included 775

sedans; 785 trucks, vans, buses; 105 fire suppression apparatuses; and 585 miscellaneous equipment items.

Fleet Management locations are spread throughout the City. There are four maintenance yards and three garages. The maintenance yards and garages are as follows:

1. Main Corporation Yard, Seventh and Taylor Streets
2. Mabury Yard, 1404 Mabury Road
3. South Yard, 4420 Monterey Road
4. West Corporation Yard, 5090 Williams Road
5. Municipal Garage, 825 North San Pedro Street
6. Airport Garage, 1395 Airport Boulevard
7. Fire Department Garage, 245 South Montgomery Street

Fleet Management's 1995-96 staffing level is 90 positions. These include 1/2 of a deputy director position; 1 fleet manager; 2 analysts; 1 automotive equipment inspector; 3 equipment maintenance supervisors; 8.5 administrative support staff; and 74 mechanics, equipment mechanic assistants, and parts workers.

The Fleet Management program budget is funded through an internal service fund. The approved budget for 1995-96 is approximately $16 million, providing $10 million for operations and $6 million for vehicle replacement, alternative fuel vehicle development, and reserves. Budgeted 1995-96 expenditures and reserves are as follows:

TABLE I

BUDGETED 1995-96 EXPENDITURES AND RESERVES

Vehicle and Equipment Operation and Maintenance		
Personal Services	$5,096,646	
Non-Personal Expenses	1,758,121	
Inventory Purchases	3,279,022	
Subtotal		$10,133,789
Vehicle Replacement and Alternative Fuel Vehicle Development		
Vehicle Replacement and Improvements	$3,403,520	
Alternative Fuel Vehicles	2,114,864	
Alternative Fuel Vehicle Fueling Station	130,000	
Subtotal		$ 5,648,384
Operating Contingency and Reserves		
Operating Contingency	$ 50,000	
Reserves (Ending Fund Balance)	363,132	
Subtotal		$ 413,132
Total		$16,195,305

Fleet Management Intends To Be Competitive

The Director of General Services issued a memorandum on June 6, 1994, explaining the department's new equipment repair rate changes. The Director also stated that General Services intended to set its rates at a level competitive with other jurisdictions and the private sector. The Director's memorandum stated in part:

> *As part of an ongoing effort to improve service delivery and to benchmark vehicle operating and maintenance charges, the Vehicle Management Program is revising its rate structure to parallel the private sector. The specific changes affecting all user departments beginning July 1994 are as follows:*
>
> - *Elimination of the "Base Rate;"*
> - *Incorporation of applicable overhead costs in a flat hourly labor rate; and*

- *Instituting a surcharge on fuel to recover overhead costs of the fuel program;*

Parts and outside costs will continue to be charged in the same manner.

The primary reason for revising the rate structure is to better enable the Vehicle Management Program to judge its competitiveness to other jurisdictions and to the private sector. Subject to changes in the Proposed Budget, the flat hourly rate is estimated to be $55 per hour. This rate is $5 to $15 less than most dealerships and outside repair shops, and will be applied to all services rendered. [Emphasis added.]

The above-mentioned memorandum shows Fleet Management's intention to be competitive by setting hourly rates that are below those in the private sector. However, our review indicated that Fleet Management has not yet established performance standards and a monitoring system to determine whether the actual hours spent for the work performed are indeed comparable to those in private industry and other governmental organizations. Fleet Management has not established such an evaluation system primarily because its current information system cannot handle the volume and/or processing of the information involved in a performance evaluation system.

Performance Standards Cannot Be Incorporated Into Fleet Management's Equipment Management Information System (EMIS)

Fleet Management currently uses the EMIS to keep track of vehicle repair and maintenance work orders, labor hours, and fuel and parts usage. The system was implemented over 15 years ago. The Fleet Management staff now considers EMIS obsolete. In a 1985 Department of General Services-commissioned study, Hughes, Heiss & Associates identified several deficiencies which prevented the EMIS from functioning efficiently (Appendix C summarizes these deficiencies.) With regard to controlling work and assessing shop performance, the consultants cited this deficiency:

EMIS does not provide a means to help shop supervisors plan and control work. Shop supervisors (as well as the Vehicle Maintenance Superintendent) lack data by which to evaluate the efficiency of their staff (such as comparisons of time spent on repairs compared to "flat rate" time). Lacking information to assess current workload levels, workload trends and shop performance, VMD supervisors and managers are placed more in reactive modes.

The Fleet Management staff agrees with this assessment. According to the staff, EMIS cannot accommodate the use of performance standards against which the system can compare actual repair times. Therefore, Fleet Management would have to manually do all of the computations and analyses required to evaluate shop performance for each repair code used on each work order for the vehicles in the fleet. Given the hundreds of thousands of individual repairs performed each year, the cost of such a manual evaluation process is prohibitive. As a result, Fleet Management has not established EMIS procedures to incorporate performance standards into the EMIS and subsequently monitor actual performance against those standards.

The Performance Standards Fleet Management Has Developed Are Not Used To Assess Fleet Management's Competitiveness With Private Industry Or Other Governmental Organizations

Fleet Management currently uses a limited number of performance standards for functions such as preventative maintenance. According to Fleet Management staff, Fleet Management developed these standards so that its maintenance supervisors could use them to train and provide guidance to employees. These standards were not intended as evaluation tools to assess Fleet Management's competitiveness primarily because the current information system (EMIS), as discussed above, cannot handle the amount of information and/or processing needed for an automated performance evaluation system.

According to Fleet Management staff, an evaluation system that can truly assess Fleet Management's competitiveness should be able to handle not only preventative maintenance functions but also the myriad repair jobs that Fleet Management performs. However, EMIS can accommodate only a limited number of repair codes. Furthermore, EMIS cannot link the repair codes to the various vehicle classes. For example, the same repair code should not be used for a brake repair job on a standard sedan and a tractor because the tractor brake job takes considerably more time. Thus, it would be wrong to evaluate a standard sedan brake job using a tractor brake job repair code, and vice versa. Given the numerous repair tasks and the variety of vehicle classes within the City, the EMIS cannot support the data processing needs of an effective vehicle maintenance performance evaluation system.

Fleet Management Needs To Formalize A Policy To Adhere To Authoritative Performance Standards Or Develop Its Own Performance Standards

Although Fleet Management has a policy to use time guides to train and provide guidance to employees, it has not formalized or documented, through a policy statement or procedures, its intention to adopt performance standards. Fleet Management has used recognized authoritative repair manuals to train its employees and provide reference materials for the vehicle maintenance staff. Of these authoritative sources one is the Mitchell Manual. Both private and public entities use this manual as a standard and/or bench marking tool in establishing their own standards to compute charges to customers. Mitchell Manual editors with extensive mechanical backgrounds in the automotive industry determine the Mitchell Manual labor time estimates. The editors determine these time estimates based on field research, time studies, and information that vehicle manufacturers supply to Mitchell.

The Mitchell Manual provides the user with detailed instructions on the following:

- Labor Times
- Overlapping Labor Times
- Additional Times
- Combinations
- Factory Times
- Hourly Rate
- Part Numbers
- Part Prices
- Mechanical Skill Level Code
- Definitions

In our opinion, Fleet Management should complete the development of a policy to adhere to recognized authoritative performance standards, such as the Mitchell Manual, or develop its own standards if authoritative standards are not available or applicable. By so doing, Fleet Management will be able to use these formally adopted performance standards not only for training but also for evaluating the performance of its staff.

We recommend that the Department of General Services/Fleet Management Division use recognized authoritative performance standards or develop performance standards for each type of vehicle maintenance or repair service.

Fleet Management Has Not Fully Implemented
Its New Fleet Management System

In 1991, General Services proposed under the Employee Innovation Program to upgrade Fleet Management's EMIS utilizing the latest fleet management technology. According to General Services, the EMIS was obsolete, cumbersome, and generated much paperwork that could be eliminated by using a bar-code system.

According to the Employee Innovation Program application, the anticipated benefit of the proposed system was to enhance fleet management by

- *Reducing paper transactions;*
- *Improving parts inventory accountability;*
- *Monitoring mechanics' labor distribution; and*
- *Tracking fleet performance by individual vehicle, vehicle class, shop facility, and division performance goals.*

Fleet Management selected, as a replacement for EMIS, a computer-based system for the management of vehicles and motorized equipment. Specifically, Fleet Management selected a Prototype Inc. product called Equipment Management System for the IBM Personal Computer Environment (EMS/PC). Among other things, EMS/PC should be capable of handling the data processing required for a shop performance evaluation system. According to the system description, EMS/PC offers the following capabilities:

- *Equipment inventory tracking, including maintenance of detailed descriptive and component data on-line;*
- *Interactive work order entry, status and tracking, with complete detail for all parts and labor charged to any task under a work order;*
- *Complete repair and preventative maintenance (PM) history data available on-line for the life of each equipment unit in both summary and detail formats;*
- *Labor analysis based on complete records for all employee labor recorded;*

- *In-depth cost analysis for operational, repair, and PM costs, including cost per mile/engine hour;*
- *Fuel and oil consumption analysis and reporting;*
- *Exception analysis and reporting of costs and fuel and oil consumption measured against user standards by equipment class (not just averages of past data);*
- *Automated PM scheduling and monitoring with special PM tasks assigned for equipment units with high costs in order to help reduce those costs;*
- *Parts and fuel inventory tracking at multiple locations with support for average, FIFO, and LIFO pricing;*
- *Purchase order tracking for parts on order with full support for blanket purchase order tracking;*
- *Usage tracking with support for rental billing to departments and agencies for equipment usage (in addition to cost billing);*
- *On-line vehicle pool reservations booking, dispatch, and tracking for multiple locations;*
- *Support for bar codes and hand-held data entry devices to capture data from both inventory and maintenance operations at maximum accuracy and minimum cost;*
- *Interface with all major automated fuel dispensing systems for processing of fuel tickets without rekeying data; and*
- *Interface files available to pass data to other systems.*

Testing and implementation of the new system started in February 1992 with the issuance of a request for proposal for the Fleet Management Software Pilot Program. In place of a separate contract for a pilot program, the City accepted from Prototype Inc. a trial period to implement EMS/PC starting in August 1992. After the trial period, the City purchased the EMS/PC program in April 1993 at a cost of $8,389. Annual software support was an additional $3,200.

Fleet Management estimates that it would cost $110,925 for the following equipment in order to implement the current version of EMS/PC. Of this amount, Fleet Management has spent approximately $79,425 as of November 1995.

TABLE II

ESTIMATED COST OF COMPUTER EQUIPMENT
TO IMPLEMENT EMS/PC

Qty	Description	Cost	Comments
1	Laitron 386DX33 8 mb 130 HD	$1,100	Prototype parts lookup
2	MIS 486 computers	2,800	Needed with or without Prototype
1	NAC 386 33 8mb 3.5" floppy	1,000	Remote dial-in
1	NAC 386sx25 4mb 3.5" floppy	800	FIRE remote access
1	NAC 386 33 16mb 1.2/1.44 mb floppy	800	Phone closet/remote access
1	Epson LQ 1170 printer	600	FIRE remote printer
1	Epson LQ 510 printer	300	ADMIN remote printer
7	Homebase for microwands	2,275	Hand-held data entry devices
50	Hand-held microwands	69,750	Hand-held data entry devices
1	ALR/HP application server	31,500	Prototype client server
	TOTAL	**$110,925**	

Fleet Management requested funding for annual hardware maintenance in its 1995-96 budget request. However, the City's Budget Office did not approve Fleet Management's request for funding. Consequently, Fleet Management has not incurred any costs for maintenance agreements for the EMS/PC system.

The original target date for implementation of the EMS/PC system was July 1993. However, due to staff reductions and the consolidation of new services into Fleet Management (such as the repair and maintenance of the Fire Department fleet), EMS/PC implementation has been delayed.

Fleet Management Should Expedite The Implementation Of The New EMS/PC

In 1978, the United States Department of Transportation, Federal Highway Administration, published an equipment management manual in which it described the importance of establishing operational goals or standards and measuring their outcome. According to the United States Department of Transportation manual,

> *The greatest value in implementing an equipment management system . . . is likely to lie in improved management understanding of established operational goals* [i.e., performance standards], *of the actions necessary to attain them* [i.e., the operational procedures], *and in the measurement of their outcome* [i.e., the performance evaluation system].

Prototype Inc., the developer and vendor of EMS/PC, also recognizes the role performance standards play in an effective fleet management system. According to the EMS/PC system description,

> *The only way to determine that a unit is not performing satisfactorily on an economic measurement is by having some standards against which to compare it. An important feature of EMS/PC, therefore, requires the establishment of standards for cost performance.*

In another section of the system description, Prototype Inc. explains the flexibility of EMS/PC in using either industry-recognized performance standards, such as the Mitchell Manual, or user-generated performance standards.

> *EMS/PC provides great flexibility in the area of standards: what you measure actual performance against. Other systems rely on national norms or a comparison against self-generated averages. With EMS/PC you choose your own standards based on what you know about your operation. We also provide tools to make standards and performance monitoring exceptionally meaningful: a tolerance percentage factor permits fine-tuning by multiple runs of exception reports. Standards also monitor employee performance and productivity on a task-by-task basis. . . .*
>
> [Y]*ou may not have any standards now and may ask, "What is the right standard?" There is no answer for that question, since there is no such thing as an objective or universal standard. A number of sets of standards have been promulgated by various organizations; and there are several flat-rate manuals available which provide repair labor hour standards for specific repair tasks on specific types of equipment.*

These standards may or may not apply to your situation. Accordingly, there are no standards embedded in EMS/PC. You must establish your own standards and load them.

Further on, the EMS/PC system description gives an example of the usefulness of performance standards in evaluating performance and controlling costs.

A similar approach is taken to the standards for labor hours on various tasks. The average time per task of each employee over a rolling twelve-month period is compared to the standard time for that task. This comparison permits you to evaluate whether an employee is performing as well as others or up to the standard. It also assists in identifying what specialties particular employees are good at--because they perform well under standard and without comebacks--and where additional training would pay off.

When Fleet Management implements the EMS/PC's performance evaluation modules, it will have a competition and costing program and be able to monitor its employees' performance against its own or industry-recognized performance standards. In our opinion, Fleet Management should expedite completing the implementation of the new EMS/PC's performance evaluation modules. By establishing performance standards and monitoring its performance against such standards, Fleet Management will be able to assess if City employees are performing effectively and competitively.

In conjunction with the performance evaluation system, Fleet Management should develop the economic benefit criteria under which a service function is to be recommended for privatization. Such criteria should address economic benchmarks or indicators so that it can be demonstrated and documented that contracting out a specific Fleet Management function or section would enhance effectiveness, efficiency, equity, or accountability. In their book, Reinventing Government: How the Entrepreneurial Spirit is Transforming The Public Sector,

David Osborne and Ted Gaebler observed that flat-out privatization is not an automatic solution.

> *Conservatives have long argued that governments should turn over many of their functions to the private sector--by abandoning some, selling others, and contracting with private firms to handle others. Obviously this makes sense, in some instances. Privatization is one arrow in government's quiver. But just as obviously, privatization is not the solution. . . . It makes sense to put the delivery of many public services in private hands (whether for-profit or nonprofit), if by doing so a government can get more effectiveness, efficiency, equity, or accountability.* [Emphasis added.]

It should be emphasized that competition, and not contracting out, is the ultimate goal of the performance evaluation system and the contracting-out criteria. The results of Fleet Management's performance evaluation system should be to document that the services Fleet Management provides to other City departments are competitive and cost effective. Only if it is economically justified based on the aforementioned economic benefit criteria should a Fleet Management function or section be recommended for contracting out. By implementing the performance evaluation system and formulating the economic benefit criteria, Fleet Management should be able to systematically analyze its performance in specific vehicle maintenance service functions or sections and identify those functions or sections that are to be recommended for contracting out.

We recommend that the General Services Department/Fleet Management Division set target dates for:

a. Completing the implementation of its new fleet management system (Prototype Equipment Management System for the IBM Personal Computer Environment);

b. Incorporating the performance standards developed in Recommendation # 1 into its fleet management system;

c. Comparing actual vehicle maintenance and repair performance to the established performance standards; and

d. Developing economic benefit criteria for recommending that vehicle maintenance and repair functions or sections be contracted out.

Our Review Of Authoritative Sources And Surveys Of Other Governmental Jurisdictions Revealed That Vehicle Maintenance Services Can Be Successfully Privatized

In the past few years, several governmental jurisdictions have made the decision to have internal service functions compete with outside vendors to provide services to other departments or citizens. This has helped to create a spirit of competition and has served to make the internal service departments more efficient and effective. Some governmental jurisdictions have gone as far as privatizing or contracting out to outside vendors for internal service department functions.

Review Of Authoritative Sources

An article titled "Opening Up the Bidding" in the November 1995 issue of Governing describes the success of the city of Indianapolis in providing its own employees the incentive to be competitive. The city of Indianapolis accomplished this by implementing the Indianapolis Competition and Costing Program. According to the article,

Initially, public employees opposed the Indianapolis Competition and Costing program. . . . In their view, the program was just another name for privatization. But after the administration assisted city workers' efforts to submit a competitive bid to repair streets -- and they won it -- the resistance began to diminish.

And it's not all that hard to see why. Activity-based costing, an accounting technique that translates every single activity and product into a dollar figure that includes indirect labor and other costs, makes managers and employees more cost-conscious by improving the accuracy of cost information and by identifying cost drivers . . . .

With a more efficient management structure and more authority over their jobs, union employees have won 80 percent of all bids for repairing potholes and road resurfacing since the program began. Two years ago, city workers won the maximum territory allowable for trash collection services. And this February, city employees beat out three national companies for a fleet maintenance and repair contract, at a savings of $8 million.

The ultimate result of introducing competition and activity-based costing in Indianapolis has been a 2 percent reduction in annual operating expenses, a 30 percent reduction in the non-public-safety work force and the identification of $123 million in savings for reinvestment in infrastructure. [Emphasis added.]

In Chapter 3 of their book, Reinventing Government: How the Entrepreneurial Spirit Is Transforming The Public Sector, David Osborne and Ted Gaebler discuss "Competitive Government: Injecting Competition into Service Delivery." They discuss how many government agencies are turning to the privatization decision to deliver more services at a lower cost. The idea is that the private sector can oftentimes provide the same level and quality of services more efficiently. The reason for the increased efficiency is not because government is inefficient. "*It is not a question of public versus private. It is competition versus monopoly.*"[1] It is not a great unknown that competition increases efficiency. With

[1] John Moffit, Chief Secretary to Massachusetts Governor William Weld.

increased competition, businesses are forced to look towards cost efficiency and customer service. The same is true for governments.

The thought has been in the past that governmental services are natural monopolies. "*It is one of the enduring paradoxes of American ideology that we attack private monopolies so fervently but embrace public monopolies so warmly.*"[2] But as the city of Phoenix found out, not all public services need to be kept in the public sector. The city of Phoenix introduced competition into certain services such as garbage collection, landfill operation, custodial services, parking lot management, street sweeping, street repair, printing, and security. The city of Phoenix invited bids in these areas from public companies and from internal governmental units. The city auditor in Phoenix estimates that installing competition into certain city services saved the city of Phoenix over $20 million over a ten-year period. The idea is not that private firms are inherently more efficient but rather that competition forces governmental units to become more efficient. Competition forces government workers to meet competitive standards or lose their jobs. The result is greater public sector efficiency.

Dr. E. S. Saves, chairman of the Department of Management at City University of New York, states that "*the most obvious advantage of competition is greater efficiency: More bang for the buck.*" According to Dr. Saves, on average, public service delivery is 35 percent to 95 percent more expensive than contracting, even when the cost of administering the contracts is included.

In the book The Privatization Decision, John D. Donahue discusses the results of a research team study the Department of Housing and Urban

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[2] Reinventing Government: How the Entrepreneurial Spirit Is Transforming the Public Sector, Osborne and Gaebler, p. 79

Development commissioned. This research team concluded that municipal agencies are 50 percent less efficient than private contractors; therefore, the average city could cut its budget for these services in half without any change in service by privatizing. In addition, the research team determined that there was "*no statistically significant difference in the quality of service provided by contractors as compared to municipal agencies . . . for any service studied.*" In fact, the team found that in each case the "*quality*" variable had no statistically detectable effect on costs at all. Therefore, the team attributes cost savings primarily to astute management practices and superior technology. Private contractors improve efficiency through more flexible use of labor, a richer array of incentives and penalties, and, often, a more precise allocation of accountability. Private contractors are less constrained by process and are more tightly focused on results.

The Department of Housing and Urban Development research team also found that contractors have three distinguishable advantages rooted in their freedom to let technical efficiency govern the size of their operations.

1. Contractors can spread the costs of capital and overhead across several cities, unlike municipal agencies which due to their size use capital equipment that is outmoded, too small, or otherwise wrong for the job. For example, the public works agencies studied tended to lack the specialized tools and labor needed for rapid traffic signal repairs. For several other services, individual cities are too small to afford an adequate inventory of spare parts and, hence, suffer from too much downtime.

2. Developing more efficient ways to deliver public services can be very costly in terms of money, time, and specialized labor, and in terms of the public disgruntlement caused by failed experiments. A private contractor, however, can claim proprietary rights to innovations, diffuse new methods

throughout its operations, and use technological advances as a competitive edge to expand its market.

3. Private contractors may be able to offer a long and flexible career ladder. This motivates workers to exert their best efforts. However, in a municipal department, advancement usually depends in large part on seniority, and room for advancement is limited by the size of the department.

While there is a considerable amount of evidence that shows that competition with for-profit rivals can dramatically boost the efficiency of public organizations, the absence of competition can just as dramatically stifle any benefits that privatization would otherwise offer.

Survey Of Other Jurisdictions

- *City of Indianapolis, Indiana*

As mentioned previously, Indianapolis, Indiana, provided an example of city employees competing against private sector companies and succeeding. The result of the competition was not only that the city employees continued to provide fleet services for Indianapolis, but the city also saved $8 million in the process. The Indianapolis Fleet Services Fact Sheet described the accomplishment:

> *In January 1995, the services of the entire operation were put out to bid and Fleet Services was successful in outbidding three private sector companies for the right to manage and maintain the City's fleet. IFS received a three year contract with two 1 year options as a result of the bid with the contract running from May 1, 1995 through April 30, 2000 (with extensions).*

It is interesting to note that the employees' union played a major role in securing the successful bid for the city employees. An April 1995 article in NAFA Fleet Executive reported,

> [John] *McCorkhill* [Administrator of Indianapolis Fleet Services] *credits Indiana Local 3131 of AFSCME, and Dominic Mangine, its president, with a*

significant role in the bid victory. "You've got to get your union working with you as a team rather than fighting and bickering with each other. By working with the union, we started empowering them and making some of the employees working group leaders. And now they actually help manage the process. Rather than a lot of foremen looking over their shoulders, we made these people responsible for getting the work done. They not only turn the wrenches but they lead and guide."

The Indianapolis Fleet Services began preparing for the competition in 1992 by "*reorganizing the department, trimming middle management and empowering employees to work in self-directed teams.*" From the beginning, it was made clear that the administration's goal was competition, not just flat-out privatization. Part of preparation for competition was the implementation of performance standards. According to the fact sheet,

Mechanics are responsible for meeting labor standards when performing repairs. Each assigned task carries with it a standard labor time that has been gathered from manufacturer's manuals governing repair; or warranty allowances; or rates that have been established through in-house time studies.

Furthermore, Indianapolis formalized the performance standards for the entire Indianapolis Fleet Service by including the performance standards in the fleet services request for proposal and the fleet services contract. These formal performance standards are described in the contract overview:

***Performance Standards**: Three main performance standards will be monitored for contract compliance:*

(1) Turnaround: The following percentages of maintenance and repair work must be completed within 24 hours of delivery to IFS.

Police vehicles (excluding confiscated vehicles)	*80%*
Fire Department vehicles	*85%*
Solid Waste trash collection vehicles	*75%*
One ton or smaller vehicles	*80%*
Larger than one ton vehicles	*75%*
All other vehicles	*75%*

Excluded from the turnaround calculations will be vehicles in the garage for accident or vandalism repairs; vehicles awaiting repair authorization by the City; vehicles needing a major component overhaul or replacement; and vehicles with a special exemption from the City.

(2) Fleet Availability: At all times 95% of every department's fleet of vehicles should be up and running. Excluded from the calculation are vehicles in the garage for "quick fix", awaiting repair authorization, user abuse, vandalism, accident, recalls, warranty work, confiscated vehicles, Acts of God or those specifically exempted by the City.

(3) Rework: No more than 15 incidents of rework will be allowed each month and all rework must be performed within 24 hours of notification.

Finally, the fleet services request for proposal required that a quality assurance program be put in place. According to the request for proposal,

The Provider will implement a Quality Assurance Program for the management of the repair and maintenance of assigned vehicles. The program will include provisions for meeting specified performance standards, for maintaining quality workmanship, for providing a high level of customer service, and for reducing fleet costs incurred by the City. The Provider will include a detailed description of its proposed Quality Assurance Program in its proposal. The plan will address, at a minimum, the following items:

- *Fleet Availability*
- *Preventative Maintenance Performance*
- *Repair Performance*
- *Parts Availability*
- *Vehicle Safety and Reliability*
- *Customer Service*
- *Cost Reduction Initiatives*

A mandatory component of the quality assurance program is user surveys. Two types will be required: (1) a survey of individual vehicle operator satisfaction each time a vehicle has been serviced, and (2) an annual user satisfaction survey of designated representatives of each user department.

- *City Of Fort Lauderdale, Florida*

In his "Contracting For Fleet Services" article published in the January 1987 issue of the APWA Reporter, the city engineer for Fort Lauderdale, Florida, said *"between 1982 and 1986, the city of Fort Lauderdale, Florida saved $1.8 million by contracting out its central garage maintenance and repair operations. These savings were in fleet maintenance, repair, and depreciation costs."* Privatization gave Fort Lauderdale the opportunity to redirect its central garage operation toward maintenance and minor repairs and away from fabrication and manufacturing. As a result, the condition of Fort Lauderdale's fleet of approximately 900 cars, light and heavy trucks, fire apparatuses, and different types of off-road vehicles has improved significantly overall with downtime reduced to 2 percent.

As the aforementioned data was somewhat dated, we called the Fort Lauderdale contract administrator to see if the city was still satisfied with its privatization decision. According to Fort Lauderdale's contract administrator, the city's overall privatization experience is still positive. The quality of service has been satisfactory. There are few complaints, and most of the customer satisfaction surveys that are returned give positive marks to the contractor. The amount of savings has not been quantified, but the staff size has been cut from 42 to 32 mechanics.

- *The City Of San Mateo, California*

The city of San Mateo, California, has a fleet of approximately 330 pieces of equipment made up mostly of cars and light trucks. City management did not necessarily start out to privatize its fleet maintenance. City management was more concerned with San Mateo's in-house service being competitive with outside private automotive repair shops. San Mateo privatized its fleet maintenance in May of 1993. The contractor is providing virtually the same level of service as was provided in-house.

The maintenance manager is the contract administrator for San Mateo. He monitors the contract on a regular basis and is the city's liaison with the contractor. His fiscal year-end report indicates a first-year savings of $163,406. This equates to a reduction of 15 percent from what vehicle maintenance was costing San Mateo prior to privatization.

Additionally, the contractor has provided very cost-effective services to San Mateo that were not part of the original contract. For example, the fire department used the contractor rather than an outside vendor to salvage and rebuild one good engine from three engines that were being removed from service. The contractor was also asked to recondition an old ladder truck so that it could be safety-certified and function as a backup piece of equipment. This was extremely cost effective because San Mateo has a negotiated fixed hourly labor rate with the contractor of $28 or less depending upon the class of mechanic needed to do the work. Market rate for the same work would have varied between $55 and $95 per hour and would have caused the fleet

maintenance modifications to double or triple in cost if San Mateo had the work done on the outside.

According to San Mateo's contract administrator, "*as confidence in the service ability of the contractor to do these more demanding jobs grows, more departments begin to use them for work that had been left pending or had formerly been done by outside vendors*." For example, San Mateo and the contractor agreed that the contractor would install communications and safety and warning equipment on police, fire, and public works vehicles rather than having an outside firm do this work. While this work was not included in San Mateo's original contract with the contractor, this service generally results in a $27 per hour labor savings to the city of San Mateo. Table III shows San Mateo's actual costs for 1993-94.

TABLE III

CITY OF SAN MATEO ACTUAL COSTS FOR 1993-94

Item	Original Estimate	Actual	Variance
Base Contract	$554,853	$535,918	($18,935)
Tires	44,000	38,280	(5,720)
Accidents or Operator Error	50,000	100,286	50,286[3]
Extras/Direct Work	12,000	93,719	81,719
Totals	$660,853	$768,203	$107,350[4]

[3] This variance resulted from San Mateo not accurately computing historical accident/operator errors costs prior to the contract.

[4] City of San Mateo Administrative Report June 15, 1994, p. 1

The San Mateo estimates it saved $163,406 in 1993-94 by privatizing its vehicle maintenance function as follows:

Total Contract Costs in 1993-94	$768,203
Add: Fuel Costs	137,891
Administrative Costs	11,500
Total All Costs	**$917,594**
Cost Analysis:	
Historical Annual Costs	$1,081,000
Total 1993-94 Costs	917,594
Savings	**$ 163,406**

San Mateo's privatization contract is a fixed-price contract. The contract is tied to the Bay Area Consumer Price Index (CPI). The Bay Area CPI rose 1.9 percent in 1993-94. Therefore, San Mateo's 1994-95 contract will not exceed the 1993-94 contract price by more than 1.9 percent.

- *The City Of Des Moines, Iowa*

The city of Des Moines, Iowa, privatized its fleet maintenance in 1983. The goal of privatization was to provide annual savings of at least 20 percent. The annually-required 20 percent savings has been realized over the eight-year life of the contract. The cost savings is the result of the private contractor, Managed Logistics Systems, Incorporated (MLS), being a more efficient operation. For example, before privatization in 1983, a staff of 72 maintained approximately 1,500 pieces of equipment. Since privatization, the number of staff has been sharply reduced to the point where currently a staff of 41 maintains over 1,600 pieces of equipment. Furthermore, Des Moines built in three benchmarks to hold the annual contract price in check.

1. The annual contract price increase for wages cannot exceed what city employees receive in contracted wage settlements;

2. Parts prices are passed through at cost with no markup; and

3. The contract target is negotiated annually and based upon actual personnel costs; other expenditures are adjusted based upon experience and as agreed to by both the contractor and the city.

We contacted the contract administrator (finance director) for Des Moines, and he told us that Des Moines has been and continues to be extremely satisfied with the contractor's service and resultant savings. The current contract cost is $3.7 million annually. Through the 12 years of the contract, savings have averaged approximately 20 percent. In 1993-94, savings were $700,000.

He stated that the quality of fleet maintenance has increased and the amount of downtime and number of vehicle breakdowns in the field have decreased significantly. He further stated that the contractor does repairs and maintenance in a timely and efficient manner and that Des Moines has had few problems administering the contract. He credits the lack of problems with the contract to the manager at the garage (an employee of the contractor). The manager ensures that all of the tasks are done efficiently and shows great flexibility in doing extra work that may not have been anticipated in the contract. Since the contract's inception, the finance director has been the contract administrator. He currently spends approximately two hours per month monitoring the contract. He conducts random spot checks of work completed. He has never found a problem.

- *Montgomery County, Maryland*

Montgomery County, Maryland, also privatized its fleet maintenance in July 1987 as a result of massive budget cuts. The county's manager of automotive equipment (contract administrator) stated there have been no significant or difficult problems to resolve with the contract.

Montgomery County's original contract included 1,325 pieces of equipment. Currently, it has approximately 1,600 pieces of equipment which include 1,200 cars, 400 light trucks, and 50 motorcycles. The contract is for three years with two, two-year extensions. The contractor is allowed to negotiate the contract on an annual basis for increases in price level or fleet size.

The current contract cost is $2.6 million annually. The manager of automotive equipment could not quantify the county's savings, but he feels it has been significant. Before the contract, 35 full-time equivalents (FTE) handled in-house fleet maintenance for 1,325 vehicles. When the contract first started, the vendor serviced the 1,325 vehicles with 24 FTEs. Currently, 20 FTEs service the fleet of 1,600 pieces of equipment. Furthermore, the contract price has remained at $2.6 million annually. Finally, the "target" contract costs have gone down each year since the start of the contract. With the contract price being held "flat" for the past eight years, the fleet size increasing by 21 percent, and 15 fewer mechanics now servicing the fleet, one can safely assume that privatization has produced substantial savings for Montgomery County.

The manager of automotive equipment has a staff of three that monitor the contract. The time he spends on the contract is minimal. Most of his time is spent on other fleet issues. He gets heavily involved in purchasing new equipment and other administrative duties. His staff consist of one technician, one administrator, and one clerk.

The technician spends 60 percent of his time monitoring the contract, an administrative person spends approximately 30 percent of her time on contract issues, and a clerk spends approximately 30 percent of her time on contract issues including overseeing the hourly leasing of motor pool vehicles.

The county's overall experience with the contractor is favorable. The service level is better than when the county provided the services in-house. The contract administrator said if he had to do it all over again, he would still privatize.

- *Los Angeles County, California*

Los Angeles County, California, privatized its fleet maintenance in 1988. Los Angeles County uses three private firms to maintain its 7,200 vehicles and pieces of equipment. The county has 4,700 pieces of equipment under a fixed-price contract and 2,500 pieces of equipment under a fee-for-service contract. The cost of the contract is as follows:

- Fixed-price portion--$11.5 million per year
- Fee-for-service portion--$3 million (most recent year)

The assistant contract administrator stated the projected savings for the seven-year contract were $10 million, or an average of $1.4 million annually. Although he would not discuss specific dollar amounts, he stated actual savings are "*somewhat under the original projections.*"

The assistant contract administrator stated he and his staff of nine do not spend all of their time monitoring the contract. The majority of their contract monitoring time is spent monitoring the fee-for-service contract. A great deal of their time is spent doing reports and special projects for supervisors and department managers.

An administrative services vendor handles such items as writing specifications and licensing vehicles, while two other vendors handle maintenance and repairs. The two vendors providing maintenance and repairs are Johnson Controls and M.P.R. Johnson Controls took over from Holmes & Narver as the major provider of fleet services. The assistant contract administrator thinks Johnson Controls is better known for providing facilities maintenance with fleet maintenance as part of the package. Johnson Controls is responsible for over 3,000 vehicles at a fixed-price contract.

The second maintenance and repair vendor is M.P.R. which is responsible for 1,650 vehicles at a fixed-price contract. M.P.R. was a local repair shop until it became a subcontractor of Holmes & Narver (the first vendor to have the contract). As M.P.R.'s work load from Los Angeles County increased, it expanded to occupy four repair facilities throughout the county.

- *The City Of Winter Park, Florida*

The city of Winter Park, Florida, privatized its fleet maintenance in October of 1991. It has 715 pieces of equipment which consist of cars, light and heavy trucks, and off-the-highway equipment.

The assistant city manager who administers the contract spends approximately one day a month doing so. The annual cost of the contract is $900,000. By privatizing its vehicle maintenance, Winter Park, Florida, has saved $350,000 annually, or 28 percent, over in-house costs.

- *Richland County, South Carolina*

Richland County, South Carolina, privatized its fleet maintenance in July of 1992. They have a fleet of 665 pieces of equipment which consists of cars, light trucks, and off-the-highway equipment.

A manager in the public works department monitors the contract. The contract administrator spends approximately five hours per month monitoring the contract. Monthly, he approves all non-contract repairs and contract items over $500 per car and light truck and $1,000 per piece of heavy equipment. The 1995-96 cost of the contract is $1,165,000. First year's savings amounted to $200,000, or 14.5 percent. The first year's savings included non-contract items; therefore, future years' savings could be even greater.

Obstacles To Privatization Such As Labor Union Resistance, Contracting-Out Pitfalls, And The City Council's Policy On Privatization Can Be Overcome

Labor Unions

Government labor unions are generally opposed to the idea of privatization and competition in government. The city of Phoenix, Arizona, addressed this problem by requiring the contractor to hire those public works employees who were displaced and transferring those who wanted to stay with the city to other jobs (sometimes at lower pay). Phoenix also discovered that competition boosts the pride and morale of public employees. The key issue of job security was solved when Phoenix adopted a no layoff policy. Once job security was no longer an issue, public employees accepted the challenge of competing with private entities.

The city of Des Moines, Iowa, also avoided employee morale problems by ensuring that no city employees lost their jobs due to privatization. Des Moines

also required the private contractor to pay comparable wages to all the employees it hired. Some of the city employees stayed on with the private contractor while the other employees were transferred to other city departments. Because both Des Moines and the private contractor's employees were unionized in the same union, there was no union objections to the privatization.

The city of San Mateo, California, avoided union concerns and employee morale issues by stipulating in its privatization contract a "*right of first refusal of employment.*" This section essentially required the contractor to offer employment to all city vehicle maintenance employees and stated in part: "*The offers of employment by the Contractor shall only be conditioned on the passage of a drug usage test and of a physical examination by the affected employees.*" Furthermore, the contract included language that provided compensation that would be equal to or more than the first step of the city's current wage scale for similar classifications.

Contracting-Out Pitfalls

Contracting out is a common method of injecting competition into public services. Writing and monitoring a public services contract must be done skillfully in order to avoid pitfalls, such as lowball bids, gradual monopolies, and fraud.

Lowball Bids - A common problem that public organizations experience when contracting out for service. The contractor bids low to get the first contract and then later raises prices. A solution is to not necessarily use the lowest bid but to use the 'lowest responsible bid.' If a company bids a contract that will generate an obvious loss or very low profit margin, chances are the bid is not a responsible bid. Another solution is to enter into long-term contracts with fixed prices that can be increased based only upon a predetermined index.

Gradual Monopoly - Another danger to be addressed when contracting out for services is that of the private contractor developing a monopoly. If a

governmental agency accepts a "lowball bid" and gets rid of its own equipment, then the contractor has effectively created a monopoly. If the contractor raises prices, it is difficult for the government organization to resume performing services in-house. Thus, the government organization is forced to pay the contractor's higher prices. The city of Phoenix, Arizona, found that the solution was to retain part of the services in-house and, if the contractor raised prices, it could simply go back to performing the contracted services in-house.

Fraud - One of the more serious dangers to contracting out for services is the danger of fraud. The solution is to ensure that

a. The bidding is truly competitive;

b. The competition is based on hard information about cost and quality of performance;

c. The contractors are monitored carefully; and

d. An impartial body is set up to perform these tasks.

The City Council's Current Policy On Privatization

On March 19, 1991, the San Jose City Council adopted Council Policy 0-24, "*CONTRACTED SERVICES.*" The purpose of this policy is to provide guidelines governing a decision to use non-City employees to deliver City service functions.

A City service function is an organized group of individuals, supplies, equipment, and facilities which the City establishes to deliver a service or services into the foreseeable future. Such a group may deliver a service to residents, to others within the same department, to other City departments, or to other public agencies.

This policy does not apply to a decision to use a contract employee to provide individual labor to the City, but it does apply to independent contractors or

firms that provide professional or consulting services. The policy states that, as a service organization, San Jose's purpose is to provide a full range of public safety, capital maintenance, and community services that are responsive, within financial constraints, to the community.

The City's policy states that City staff will deliver the desired day-to-day level of all City services. The policy lists eleven specific exceptions, eight specific conditions, and four specific decision criteria for using contract services. The current policy does not allow contracting out purely for economic reasons as an exception to its City staff requirement. In other words, the City must use City staff to provide City services even if a private entity can provide the same service for less cost. Therefore, until Council Policy 0-24 is revised to allow contracting out for economic reasons, privatizing is not an available option for more efficient and effective operation of a City department, program, or division. A complete text of Council Policy 0-24, is included in this report as Appendix E.

We recommend that the San Jose City Council amend Council Policy 0-24 to add demonstrated economic benefit to the city of San Jose as an exception to its City staff delivering a service function.

CONCLUSION

Our review of Fleet Management's system for developing and using performance standards and for determining whether its performance is competitive with private industry and other governmental organizations revealed that

- Performance standards cannot be incorporated into Fleet Management's Equipment Management Information System (EMIS). As a result, Fleet Management has no procedures to either incorporate performance standards into the EMIS or monitor actual performance against established performance standards;
- The performance standards Fleet Management has developed are not used to assess Fleet Management's competitiveness with private industry or other governmental organizations; and
- Fleet Management has not fully implemented its new fleet management system.

In addition, with regard to privatizing the vehicle maintenance function,

- Our review of authoritative sources and surveys of other governmental jurisdictions revealed that vehicle maintenance services can be successfully privatized and
- Obstacles to privatization, such as union resistance, contracting-out pitfalls, and the City Council's current policy on privatization can be overcome.

In our opinion, Fleet Management should expedite the implementation of its new Equipment Management System for the IBM Personal Computer Environment (EMS/PC). By establishing performance standards, developing economic benefit criteria for recommending privatization, and monitoring actual performance against those standards and criteria, Fleet Management will be able to assess if it is

functioning economically, efficiently, and effectively and to identify the functions that can be successfully privatized.

RECOMMENDATIONS

We recommend that the Department of General Services/Fleet Management Division:

Recommendation #1:

Use recognized authoritative performance standards or develop performance standards for each type of vehicle maintenance or repair service. (Priority 2)

Recommendation #2:

Set target dates for:

a. Completing the implementation of its new fleet management system (Prototype Equipment Management System for the IBM Personal Computer Environment);

b. Incorporating the performance standards developed in Recommendation #1 into its fleet management system;

c. Comparing actual vehicle maintenance and repair performance to the established performance standards; and

d. Developing economic benefit criteria for recommending that vehicle maintenance and repair functions or sections be contracted out. (Priority 2)

Finally, we recommend that the San Jose City Council:

Recommendation #3:

Amend Council Policy 0-24 to add demonstrated economic benefit to the city of San Jose as an exception to its City staff delivering a service function. (Priority 3)